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AGENDA ITEM 9

TO: MEMBERS OF THE FINANCE COMMITTEE

- I. SUBJECT:** CalPERS 2008-11 Three-Year Business Plan Semi-Annual Update
- II. PROGRAM:** Systemwide
- III. RECOMMENDATION:** Approval of changes to the CalPERS 2008-11 Three-Year Business Plan and transmittal to the Legislature as specified below.
- IV. ANALYSIS:**

The CalPERS Board of Administration formally adopted the CalPERS Three-Year Business Plan (Attachment A) in April 2008. The plan includes business objectives targeted for fiscal years 2008-09 through 2010-11. This agenda item provides the second semi-annual update on the plan, as well as recommended changes to two of the 37 objectives.

Upon approval by the Board of Administration, the 2008-11 Three-Year Business Plan Semi-Annual Update will be transmitted, via the attached transmittal letter (Attachment B), to the Joint Legislative Budget Committee, Fiscal Committees of the Legislature, the State Controller, and the Department of Finance in accordance with the Budget Act of 2008; and the Legislative Analyst's Office and the State and Consumer Services Agency.

Completed Three-Year Business Plan Objectives

This semi-annual update reflects the progress and status of CalPERS 2008-11 Three-Year Business Plan objectives from July 1, 2008, through December 31, 2008. During this period, nine business objectives with a December 31, 2008 due date were completed.

The Three-Year Business Plan status is as follows:

Goal II. Foster a work environment that values quality, respect, diversity, integrity, openness, communication, and accountability.

Objective #2.6 – By December 31, 2008, establish a comprehensive enterprise wide diversity awareness baseline.

- **Completed** – The CalPERS Board recognized diversity as a critical business issue in 2006 with the creation of the CalPERS Diversity Outreach Program (CDOP) and the inclusion of diversity in our Strategic Plan. This objective calls for the development of a diversity awareness baseline to measure the effectiveness of ongoing program outreach initiatives.

During 2008, CDOP conducted an awareness survey for CalPERS employees. The survey collected awareness data on a variety of diversity issues and programs, including understanding and commitment to diversity, fair people processes, business impact, valuing differences, and inclusion. Based on an analysis of survey results, the CalPERS diversity awareness baseline was established at 60 percent.

Future diversity awareness and inclusion strategies will focus on improving the baseline by 5 percent by December 2010, as called for in Objective 2.7.

Objective #2.8 – By December 31, 2008, develop and implement a comprehensive diversity strategy that is integral to our external programs and that seeks to take advantage of all the skills, talents, and opportunities within the marketplace.

- **Completed** – The CalPERS Diversity Program Overview and Action Plan was presented to the Board in October 2008. This strategy calls for enhancing relationships and alliances with internal and external stakeholders and business partners; expanding diversity information reporting; and increasing outreach activities.

Board discussions on this strategy are still in progress, but several initiatives have been implemented to date. These include the recently held Women in Investments Conference, the launch of a new internal Web site, partnering with the Operations Support Services Division to advance supplier diversity, and creating Web access for external business partners.

Goal III. Sustain a high performance work culture utilizing staff development, technology, and innovative leadership and management strategies.

Objective #3.2 – By December 31, 2008, all managers will know of and have the opportunity to participate in the Succession Planning Framework to sustain current leadership, develop new leaders, and maintain the intellectual and human capital of CalPERS.

Completed – A Succession Planning Framework was implemented, introducing new training and tools available to CalPERS leaders at all levels.

Leadership learning strategies implemented include a Workforce Planning Workshop for managers and supervisors; the launch of an online “onboarding” tool to help acclimate new employees to the CalPERS organization; a Leadership Acceleration Workshop to increase strategic thinking skills and business acumen among future leaders; the 360° Leadership Feedback to provide managers and supervisors with constructive performance feedback and personal coaching; and expansion of the L.E.A.D.E.R. training series to advance ongoing leadership development.

In addition, to support succession planning, an “InfoMapping” documentation process, software, and training were introduced to provide an enterprise methodology for standardizing and institutionalizing CalPERS business processes, procedures, and other information assets.

Goal V. Provide sustainable pension benefit products and services responsive to and valued by members, employers, and stakeholders.

Objective #5.1 – By December 31, 2008, establish a Board approved methodology for our employers, members and their representatives, and stakeholders to use when designing and selecting benefits.

- **Completed** – The Chief Actuary has developed a report on the methodology for this objective, which will be reported to the Board under separate cover.

Goal VI. Administer pension benefit services in a customer oriented and cost effective manner.

Objective #6.4 – By December 31, 2008, establish target per unit pension transaction costs.

Completed – The intent of this objective was to set operational improvement targets that could be used to measure efficiencies realized by the new PSR technology infrastructure. PSR has redefined the future CalPERS business environment and improvements will be realized in increased efficiencies across the board, rather than a cost per transaction basis.

The PSR project has established a series of success criteria and performance measures that do not tie to cost per transaction measures, negating the ability to measure costs before and after system launch.

To align the objective's intent for operational efficiencies with the change in CalPERS business direction, three of the PSR metrics have been identified as appropriate targets. They include increased online transactions for both members and employers, and the reduction of time spent on manual reconciliation.

Goal IX. Achieve long-term, sustainable, risk adjusted returns.

Objective #9.1 – By December 31, 2008, identify and implement new investment strategies and opportunities to enhance long-term, sustainable returns and provide the Investment Committee with a report documenting their value added and cost effectiveness.

- **Completed** – The Investment Office has implemented several new investment strategies and opportunities, including new Global Equity Internally Managed Portfolios for International Small and Micro Cap and Emerging Markets; the recently implemented Inflation-Linked Asset Class; and the Active Currency Initiative.

Changes to the Credit Enhancement Program were approved by the Investment Committee in June 2008, increasing the total aggregate commitment amount from \$5 billion to \$10 billion and eliminating the dollar-based transaction limit; a strategy was completed to restructure the products offered in the Supplemental Income Plans creating a more competitive list of products; and the Investment Office also partnered with the CalPERS Information Technology Services Branch to create a new structure to support investment technology needs.

Objective #9.2 – By December 31, 2008, execute the Board approved strategic initiatives to improve transparency, shareowner rights, and board accountability, including shareowner access to proxy, executive compensation practices, environmental disclosure, and majority vote standards.

- **Completed** – The Investment Office successfully executed several Board-approved strategic initiatives through company engagement, including six portfolio companies declassifying their board of directors; eight others adopting a majority vote provision for director elections; and 47 portfolio companies either disclosing existing, or implementing new, executive compensation clawback policies. Staff successfully achieved majority vote support from shareowners on one portfolio company for an executive compensation Advisory Vote standard which subsequently led to adoption by the company. The CalPERS Global Principles for portfolio companies were also revised to focus on the importance of pay-for-performance executive compensation practices, financial statement integrity, environmental disclosures, and the diversity of corporate Boards.

In addition, Investment Office representatives met with members of Congress to share the CalPERS corporate governance policies on promoting proxy access, majority vote provisions, executive compensation, and environmental disclosure. And, our corporate governance efforts through the CalPERS Focus List Program not only catalyzed improved corporate governance best practices, but continued to demonstrate excess economic return to the CalPERS Investment program as measured by Wilshire Associates' study, "The CalPERS Effect."

Objective #9.3 – By December 31, 2008, develop and implement a comprehensive diversity strategy that is integral to our investment program and that seeks to take advantage of all the skills, talents, and opportunities within the marketplace.

- **Completed** – The Investment Office successfully implemented a comprehensive diversity strategy that focuses on expanding business opportunities for emerging managers and increasing access to information that would facilitate future collaboration.

The Investment Office has developed new programs, and expanded existing programs, to take advantage of new perspectives in the investment arena. Both the Emerging

Manager Fund of Funds, and the Fund of Emerging Hedge Funds are new efforts designed to seek out emerging managers

with competitive ideas and strategies. In addition, the Alternative Investment Management Program and their California Initiative have significantly expanded investments with diverse partners. The California Initiative provides capital to companies with diverse management, employees from low- to moderate-income areas, and difficulty accessing capital from traditional sources. The Alternative Investment Management Program also committed \$400 million to a private equity fund of funds for emerging managers.

CalPERS, working with CalSTRS, created the first-of-a-kind database of emerging managers and financial service providers. In building the diversity database, CalPERS created a platform that not only stored data, but allowed for capabilities that would facilitate research, analysis, and networking. This information will be leveraged by Investment staff to expand the diversity of ideas and people in their investment portfolios, and the investment portfolios of other institutional investors. The diversity database bridges the existing information, knowledge, and collaboration gaps in the emerging manager space and provides all of the CalPERS investment staff access to an extensive resource.

The Investment Office continues to support the CalPERS commitment to diversity through the recruitment and retention of diverse Investment staff. By leveraging relationships with the Toigo Foundation and other university-sponsored programs, the Investment Office has made efforts to engage a growing community of potential talent.

Goal X. Develop and administer quality, sustainable health benefit programs that are responsive to and valued by enrollees and employers.

Objective #10.2 – Annually maintain the number of contracting agencies at or above 98 percent of 2006 levels.

- **Completed** – During 2008, the Health Benefits Branch continued proactive recruitment and retention strategies to attract new contracting agencies and retain existing agencies. CalPERS health plan cost containment strategies over the past three years contributed to our ability to offer a desirable, marketable health benefits package that assisted staff in both retaining existing employers and recruiting a number of new public agencies and schools.

Personalized outreach efforts were conducted that focused on 22 “at-risk” contracting agencies that represented the potential loss of more than 16,000 total covered lives. Numerous discussions with employers, special presentations, and phone conferences were conducted throughout 2008, resulting in only three of those agencies and three employee groups electing to cancel their CalPERS health contracts.

As a result of their efforts, the Health Benefits Branch retained 99.7 percent of the public agencies and school districts in the Health Benefits Program. And, 17 new agencies established contracts adding more than 9,000 covered lives, and six existing agencies added eight new employee groups with approximately 900 covered lives.

Proposed Business Plan Objective Changes

Due to external business events that continue to impact our ability to complete the following business plan objectives, changes to the target dates are recommended. Changing the dates will ensure both objectives are executed in tandem which was the intent when they were developed.

Goal XII. Engage and influence the healthcare marketplace to provide medical care that optimizes quality, access, and cost.

Objective #12.1 – By December 31, 2008, consistent with the CalPERS “Partnership for Change,” maintain publicly available standardized hospital quality and cost efficiency data to help make informed health care decisions.

- **Partially Completed / Revise Target Date** – As reported to the Board in February and September 2008, this objective has been partially completed. Comprehensive report cards on quality of care, patient satisfaction, and safety measures were released on a public Web site in March 2007. However, the cost data also required by this objective is on hold pending Department of Justice resolution of anti-trust issues. Once those issues are resolved, the Hospital Value Initiative (HVI) project will re-engage with hospitals and the California Hospital Association to move forward. At this time, it is recommended the target completion date for this objective be changed to December 31, 2010.

Objective #12.2 – By December 31, 2008, increase the number of purchaser covered lives (i.e., number of covered lives represented by the organizations in the Partnership) endorsing the CalPERS “Partnership for Change” to 6 million.

- **Revise Target Date** – As reported to the Board in February and September 2008, this objective has also been impacted by the delay in the Department of Justice anti-trust decisions. To provide adequate time to effectively implement Objectives 12.1 and 12.2 as intended, both the California Hospital Assessment and Report Task Force and the HVI project must be operational. Once this occurs, recruitment efforts to increase the number of members endorsing the Partnership for Change can resume. At this time, it is recommended the target completion date for this objective be changed to December 31, 2010.

Objective Status Reporting Tool

The Three-Year Business Plan Objective Summary “stoplight” dashboard was introduced to the Finance Committee in September 2008 to provide the Board with an additional tool to monitor plan progress.

The current business plan objective status dashboard (Attachment C) is included in this agenda item for your review. The summary employs green, yellow, and red stoplights, which are defined as:

- Green – On target or trending to target.
- Yellow – Need to watch trend.
- Red – Management attention needed.

Currently, Objectives 12.1 and 12.2 are reporting as red due to their December 31, 2008 target dates. Approval of the above recommendation to change the target dates to December 31, 2010, would also change the reporting status to green.

All remaining business plan objectives are on target and are reporting as green.

Conclusion

Of the 37 objectives in the CalPERS 2008-11 Three-Year Business Plan, 14 have been completed, and changes have been recommended for two objectives.

Work related to the three objectives with an upcoming July 1, 2009, target date is in progress. The status of these objectives, as well as the stoplight dashboard for all objectives, will be reported at the September 2009 Finance Committee meeting.

V. RESULTS/COSTS:

Cost and resource needs associated with the projects and other activities identified in the Three-Year Business Plan have already been allocated.

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Attachments